

COUNTY OF MILWAUKEE
Inter-Office Communication

Date: October 24, 2005

To: Supervisor Richard D. Nyklewicz, Chairman, Finance and Audit Committee
Supervisor James J. "Luigi" Schmitt, Chairman, Personnel Committee

From: Jerome J. Heer, Director of Audits
Charles McDowell, Director, DAS-Division of Human Resources
Steve Cady, Fiscal and Budget Analyst, County Board Staff
Rick Ceschin, Policy Research Analyst, County Board Staff

Subject: Comparison of Employee Health Care Models Employed by Milwaukee County, the City of Milwaukee and the State of Wisconsin [File No. 05-382].

On July 28, 2005 the Milwaukee County Board of Supervisors approved a resolution authorizing and directing the Director, Department of Administrative Services—Division of Human Resources, the Director of Audits and County Board Staff (Work Group):

"...to review and compare the employee health care models provided by the City of Milwaukee and State of Wisconsin to determine if additional cost savings could be achieved if a similar approach was implemented for Milwaukee County; and

...that the Work Group shall also examine whether any opportunities exist for Milwaukee County to partner or participate in the health care plans provided by the City of Milwaukee or State of Wisconsin...."

Background

State of Wisconsin Model

The State of Wisconsin has used a managed competition approach to its employee health insurance program since 1984. As originally designed, the program provided incentives for employees to choose lower cost providers by establishing the lowest-cost provider as a 'free' (no premium cost share) option and increasing the employee's share of premium cost for higher cost providers. Beginning in 2004, the State embarked on a new approach to generate additional reductions in costs. Under the new 'three tier' method, plan providers are placed in one of three categories with Tier 1 being the least expensive for employees and Tier 3 being the most expensive. The individual health plans are placed into one of the three tiers based on the efficiency and quality of care the plan provides to members. Providers wishing to gain higher levels of employee participation have an incentive to be included in ***Tier 1***. All tiers have the same benefit level. The process for categorizing providers is driven by actuarial data, and providers are provided an opportunity to adjust pricing so they can be placed in a lower tier.

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City of Milwaukee Model

The City of Milwaukee uses a modified version of the three-tiered health plan to apply downward pressure on plan costs. The City offers both Health Maintenance Organization (HMO) plans and the more traditional patient-choice style plan known as the Basic Plan. The two HMO plans offer 'uniform benefits' and differ only in terms of network breadth. The Basic Plan consists of three benefit levels – Basic Plan, Basic Plan **Tier 1** and Basic Plan **Tier 2**. The Basic Plan is reflective of a more traditional Preferred Provider Organization (PPO) structure, while Tiers 1 and 2 offer differing networks with higher out-of-network patient costs.

In general, and conditional on bargaining unit status, the City will pay the full monthly premium of the lowest cost HMO plan, and will contribute that amount toward subsidizing the monthly premium of any other offered plan. Participants who wish to enroll in a broader HMO network, the Basic Plan or the Basic Plan Tiers are required to pay the difference in premiums via payroll deduction.

Under this structure, potential plan vendors have the knowledge that their product may be available at no cost to employees and are therefore more likely to attract participants.

Milwaukee County Model

Milwaukee County has traditionally offered a choice of health plans to its employees and covered retirees. The Milwaukee County Conventional Health Care Plan (Conventional Plan) has been a self-funded, comprehensive fee-for-service health care plan administered by a Third Party Administrator (TPA). Over the years, one or more fully-insured plans administered by various (HMOs) have also been offered. While benefits are similar under the alternative plans, HMO coverage has generally been provided with relatively fewer or lower patient co-pays, and with greater restrictions on health care provider choices, than the Conventional Plan.

Periodically the County has accepted competitive bids for both the self-insured (Conventional Plan) and fully-insured (HMO) health care plans. For the first time in 2003, Milwaukee County contracted directly with a single health care provider (Aurora Health Care Systems) on a fee-for-service basis. This was in addition to its traditional Conventional Plan and HMO arrangements.

For 2006, Milwaukee County has converted the self-funded Conventional Plan to a fully-insured, premium-based health care plan administered by Wisconsin Physicians Service (WPS).

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Health Care Plan Benefits

A general comparison of the benefit structure of the basic health care plans offered by Milwaukee County, the City of Milwaukee and the State of Wisconsin are provided in *An Audit of the Milwaukee County Employee Health Care Benefit (June 2004)*. The report details differences in cost-sharing features including contributions towards premiums, deductible and co-insurance amounts, as well as co-pays and annual out-of-pocket limits. However, major areas of coverage are substantially similar among the three entities' health care plans.

Cost Comparison

We compared health care cost data compiled by each of the three entities for the five-year period 2001 through 2005, using budgeted figures for 2005.

Gross Cost Comparison

The information presented in **Table 1** (attached) represents gross health care expenditures by the three entities, exclusive of employee and/or retiree premium contributions. The gross cost information includes actual health care claims payments and direct administrative fees for the self-insured aspects of each entity's health care plan, as well as total premiums paid for the fully-funded HMO coverages offered. The Milwaukee County and City of Milwaukee data includes the cost of Medicare premiums paid on behalf of covered retirees (Milwaukee County pays 100% of covered retirees' Medicare premiums; the City of Milwaukee pays 25%). Offsets from employee and, in the case of the City of Milwaukee, retiree contributions to premiums are not included in the gross cost data shown in **Table 1**.

Table 1 shows that for the most recent five-year period, on a per contract (subscriber) basis, average annual gross costs for the three entities were very close in four of the five years. During the first four years of the period, the difference between the lowest- and highest-cost entity ranged from 1.3% to 4.7%. In the fifth and most recent year, the differential increased to 12.4%. It is interesting to note that Milwaukee County's average gross cost per contract was the lowest among the three entities in 2001 and 2003, while the State achieved that distinction in 2002 and 2004. In addition, the State will have the lowest gross average in 2005, based on budgeted figures.

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As previously noted, the State revised its managed competition model in 2004. Prior to that time, the State would provide, free of any employee premium cost share, health care plans whose premiums were within 105% of the lowest cost plan bid in open competition. The State included additional plans as options for employees, but any premium cost above 105% of the lowest cost option had to be paid by the subscriber. In 2004, the State modified its approach, allowing more than one provider to attain the designation of a **Tier 1** health care provider (nominal premium contribution on the part of employees), even though the State may pay different premium amounts to different providers in the same tier. Discussions with State plan administrators indicate this model revision allowed for more flexibility to apply downward pressure on providers in the negotiation process, because providers realized they stand to lose significant market share if they fail to reduce premiums sufficiently to attain the **Tier 1** designation. Allowing for more than one provider to achieve the **Tier 1** designation without exactly matching the 'low bid' provides leverage for the State to squeeze more efficient rates out of providers with different cost factors.

A recent announcement by the State that 2006 health care premiums are expected to increase a relatively low 9.6% over 2005 premiums are a further indication that the State's managed competition model may be effective in placing downward pressure on spiraling health care costs.

Demographic Data

One of the major cost drivers in health care is the average age of the insured population. According to data provided by the three entities, the demographics of subscribers (not including dependents) is as follows:

	<u>City of Milwaukee</u>	<u>Milwaukee County</u>	<u>State of WI</u>
Average Subscriber Age	57.1	58.8	49.6
Percent Retirees	41%	57%	21%

The average age of subscribers suggests that, while the City of Milwaukee and Milwaukee County insured population is relatively similar in age, the State of Wisconsin had a much lower average subscriber age. In general, this would have a depressing influence on health care costs in comparison to the City of Milwaukee and Milwaukee County.

Net Cost Comparison

Table 2 (attached) presents the same cost data as **Table 1**, but includes the impact of employee and covered retiree contributions to health care premium costs. This net cost comparison clearly

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shows that the City of Milwaukee passes a greater percentage of its health care costs onto employees and covered retirees.

For instance, as budgeted for 2005, the City of Milwaukee has shifted approximately 23% of its health care costs to employees and covered retirees, reducing its gross health care costs from \$10,258 per contract to \$7,684. By contrast, Milwaukee County shifted approximately 6% of health care costs to employees and covered retirees, reducing its budgeted gross health care costs for 2005 from \$10,672 per contract to \$10,041 per contract. Comparable data for the State shows a cost shift of about 7%, reducing the State's budgeted gross health care costs for 2005 from \$9,495 per contract to \$8,859.

Thus, while the average gross health care expenditures for Milwaukee County, the City of Milwaukee and the State of Wisconsin are relatively close, the greater proportion of cost-shifting engaged by the City of Milwaukee creates a significant difference in average net health care expenditures. Thus, while the City of Milwaukee and Milwaukee County gross health care costs per contract are very similar, the City's net health care costs per contract are 21.7% lower than the County's for 2005.

Implications for Milwaukee County

Obstacles to Merging with City or State.

The June 2004 health care audit identified several obstacles confronting different government jurisdiction wishing to coordinate efforts to acquire health care services. Pooling purchasing power with other public entities to increase market leverage and obtain greater provider discounts is often suggested as a logical idea to reduce the cost of health care. However, in discussing this matter with the health care staff of local jurisdictions and health care consultants, the realities of such a joint venture make it difficult to implement.

Some of the problems of such an undertaking include:

- The involvement of several different collective bargaining units with different contract expiration cycles.
- Pre-existing provider preferences based on past experiences.
- Different workforce demographics and plan characteristics that could make uniform provider pricing difficult. In effect, some jurisdictions could end up subsidizing others.

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While these difficulties are not necessarily insurmountable, overcoming them would require mustering the political will to bring many divergent interests together. Consequently, we view this as a potential long-term strategy worth exploring, but not practical in the near term.

Further, attempting to join the State of Wisconsin plan, currently available only to municipalities that participate in the State Employee Retirement System, would require a change in State Statutes.

Adaptability of Key Features

State administrators acknowledged that its managed competition model has not worked well in Milwaukee County due to a concentration of market power in hands of providers in the Milwaukee area. As one State administrator put it, "every provider is in every network." To combat this, the County likely would have to apply the managed competition model concept at the provider level, rather than at the network (Third Party Administrator) level. This would involve establishing a bidding process whereby individual hospital-based systems, or consortium of systems, bid for exclusive rights to provide health care for Milwaukee County employees and covered retirees. In such a scenario, a number of local providers would likely be 'shut out' from County business unless they embraced a truly competitive rate structure. In theory, the approximately \$120 million in health care expenditures generated by Milwaukee County should be sufficient to drive current high-cost providers either out of the market, or into a more competitive rate structure.

Other Factors

Milwaukee County has recently entered into a health care contract with Wisconsin Physicians Service (WPS) that converts the historically self-insured Conventional Plan option to a fully insured health care plan. In addition, one Milwaukee County collective bargaining unit (the Deputy Sheriff's Association) has agreed to, and several collective bargaining units have tentatively agreed to, major plan design changes in the Conventional Plan option that significantly increase employees' share of health care costs. Further, with a somewhat unlikely opt-out contingency in the third and fourth year, the WPS/Milwaukee County contract is, for all practical purposes, "locked in" for four years. Thus, while a modified managed competition model holds some promise for success in Milwaukee County, the first opportunity for implementation of such an approach would likely be 2010. The long lead time for implementation would provide Milwaukee County with the opportunity to gear up resources to accomplish this change in approach, which would require a combination of staff and consultants with the proper skill mix—a small team of analysts, as well as a team of negotiators.

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Given the fast pace of changes in the health care industry, it is recommended that this report be received and placed on file, with a commitment from the Division of Human Resources to review the potential benefits of adopting a modified managed competition model of health care acquisition, or a change in State law permitting County participation in the State plan, when a decision point on renewing the current WPS contract nears.

Jerome J. Heer
Director of Audits

Charles McDowell
Director, DAS-Division of Human Resources

Steve Cady
Fiscal & Budget Analyst

Rick Ceschin
County Board Research Analyst

DCJ/cah

cc: Supervisor Lee Holloway, Chairman, Milwaukee County Board of Supervisors
Milwaukee County Board of Supervisors
Scott Walker, Milwaukee County Executive
Terrence Cooley, Chief of Staff, County Board Staff
James Villa, Chief of Staff, County Executive's Office
Linda Seemeyer, Director, Department of Administrative Services
Stephen Agostini, Fiscal and Budget Administrator, DAS
Laurie Henning, Chief Committee Clerk, County Board Staff

Attachment

Table 1
Gross Cost Analysis: Milwaukee County, City and State Health Care Cost Info 2001—2005

Milwaukee County				City of Milwaukee			State of Wisconsin			Comparisons				Year
Year	Contracts	Per Cont.	Annual Increase	Contracts	Per Cont.	Annual Increase	Contracts	Per Cont.	Annual Increase	Per Contract Cost		% Difference		
										Lowest	Highest	Highest vs. Lowest		
2001	10,939	\$6,351		12,197	\$6,435		82,510	\$6,421		County	City	State 1.3% > Co.	2001	
2002	10,895	\$7,444	17.2%	11,966	\$7,574	17.7%	84,666	\$7,338	14.3%	State	City	City 3.2% > State.	2002	
2003	10,550	\$8,090	8.7%	11,770	\$8,270	9.2%	86,701	\$8,193	11.7%	County	City	City 2.2% > Co.	2003	
2004	10,597	\$9,451	16.8%	11,649	\$9,064	9.6%	87,242	\$9,024	10.1%	State	County	County 4.7% > State	2004	
2005	10,591	\$10,672	12.9%	11,477	\$10,258	13.2%	87,180	\$9,495	5.2%	State	County	Co. 12.4% > State	2005	
Avg. Increase '01-'05			13.9%	Avg. Increase '01-'05			12.4%	Avg. Increase '01-'05			10.3%			
5-Yr. Total		\$42,008		5-Yr. Total		\$41,601		5-Yr. Total		\$40,471	Five-Yr. Avg. Total: Co. 1% > City; City 2.8% > State			

Source: City of Milwaukee Dept. of Employee Relations, State of Wisconsin Dept. of Employee Trust Funds and Milwaukee County Annual Budgets

Table 2
Net Cost Analysis Milwaukee County, City and State Health Care Cost Info 2001—2005

Milwaukee County						City of Milwaukee			State of Wisconsin			
Year	Gross Cost	Net Cost	Contracts	Per Cont.	Annual Increase	Contracts	Per Cont.	Annual Increase	Contracts	Per Cont.	Annual Increase	
2001	\$66,579,849	\$63,903,537	10,939	\$5,842		12,197	\$4,862		81,510	\$5,892		
2002	\$78,167,135	\$74,063,716	10,895	\$6,798	16.4%	11,966	\$5,970	22.8%	84,666	\$6,752	14.6%	
2003	\$81,547,156	\$78,596,934	10,550	\$7,450	9.6%	11,770	\$6,185	3.6%	86,701	\$7,569	12.1%	
2004	\$96,126,125	\$94,495,413	10,597	\$8,917	19.7%	11,649	\$6,972	12.7%	87,242	\$8,367	10.5%	
2005	\$108,412,669	\$106,342,805	10,591	\$10,041	12.6%	11,477	\$7,864	12.8%	87,180	\$8,859	5.9%	
Avg. Increase '01-'05					14.6%	Avg. Increase '01-'05			13.0%	Avg. Increase '01-'05		10.8%

Source: City of Milwaukee Dept. of Employee Relations, State of Wisconsin Dept. of Employee Trust Funds and Milwaukee